Colombia's Rise:
A Primer for International Investors

January 2013

PARKMADISONPARTNERS

TABLE OF CONTENTS

For much of the past year, Park Madison Partners has been conducting due diligence on the emerging real estate opportunity in Colombia. We have toured assets; met with local investors and government officials; attended seminars; and combed through books, articles, and presentations. As is the case with any market, one cannot form a reliable view on Colombia's real estate market without first understanding the broader story of the country itself. In this briefing, we have attempted to outline our findings on Colombia's economy, history, and culture – and how they relate to the investment opportunity in the country today.

OVERVIEW AND DEMOGRAPHICS

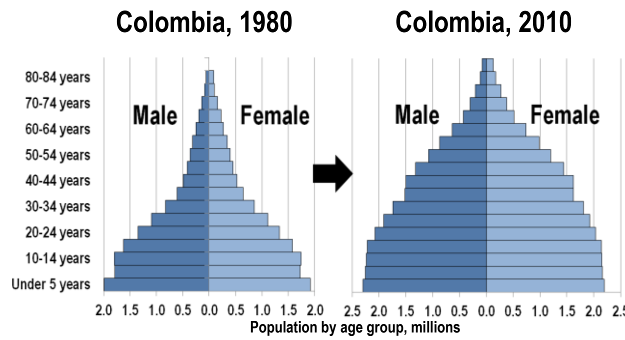
Strong economy in an institutional-sized market

The Republic of Colombia is one of the oldest democracies in Latin America, having won independence from Spain in 1819. With a population of 46.9 million, Colombia has the third largest population in Latin-America, after Brazil and Mexico. Colombia covers almost twice the land area of France, and is the 26th largest country in the world.

As of 2011, Colombia was the 29th largest economy in the world with nominal GDP of US$471 billion. 2011 purchasing power increased 5.7% in real terms over 2010, and growth has averaged approximately 4.5% annually since 2002. Major exports include oil, coal, coffee, cut flowers, textiles, processed food, shoes, and cement.

Growing labor force and emerging middle class

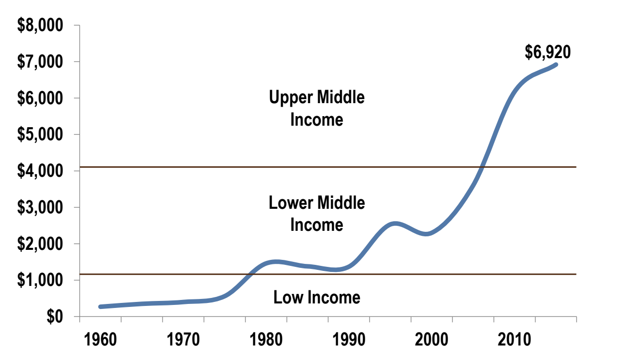
Census data suggests Colombia's population growth has averaged 1.5% annually over the past decade. Colombia has a relatively young population, with a median age of 28.3 years despite a life expectancy of 75. Like other emerging economies, this is expected to fuel a "demographic dividend" as the working age population becomes a larger percent of the total. Colombia currently enjoys the 5th highest labor force growth rate in the world, which points to major productivity gains ahead.



Source: United Nations, Population Division. 2012.

The benefits of Colombia's maturing demographics are also visible in the growth of the nation's middle class. 2011 per capita GDP is up 60% versus 2000 levels. Per capita GNI, which is considered more accurate than GDP for measuring living standards, surpassed the US$4,000 level in 2006, which places Colombia in the "upper middle income" category based on World Bank ratings. This income level is thought to represent the threshold beyond which consumers can begin spending more on retail and housing, rather than purely subsistence items.

Gross National Income per Capita (2011 US$ millions)



Source: Ministerio de Hacienda y Crédito Público; EIU; ProExport Colombia. 2012.

GEOGRAPHY

Highly urbanized population

While Bogotá is by far the largest metropolis in Colombia, there are several major urban centers throughout the country. With an urbanization rate of 75% and projected to rise, Colombia now has four cities with populations larger than 1 million, 22 cities larger than 300,000, and 57 cities larger than 100,000. Most of Colombia's cities and about 90% of the population are located either in the Andes Mountains or along the Caribbean coast.

City	Population	% of Total
Bogotá	8.9 million	20%
Medellín	2.7 million	6%
Cali	2.2 million	5%
Barranquilla	1.1 million	2%
Colombia Total	**45.2 million**	**100%**

Source: DANE (National Department of Statistics). 2011.

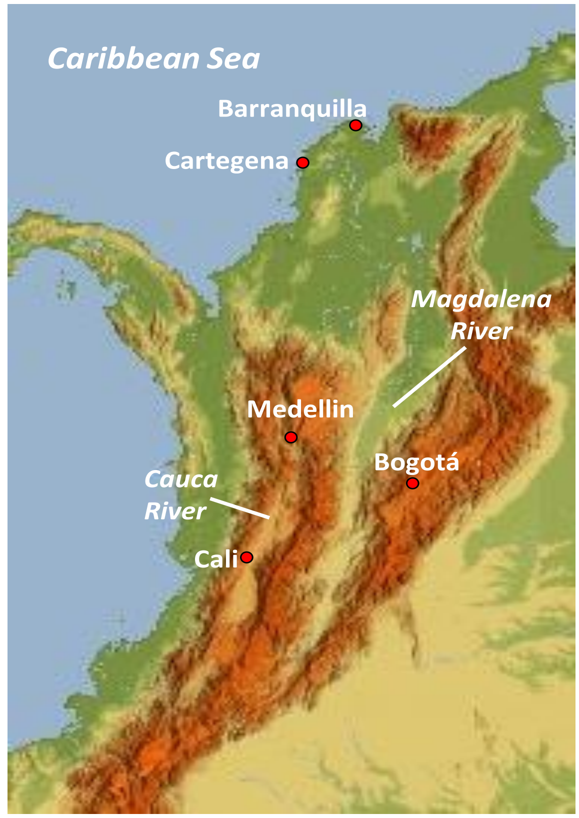
Challenging effects of geography and climate

The diversity and challenges of Colombia's geography have caused it to play an outsized role in shaping the country's history, politics, and culture. Broadly speaking, the landscape is dominated by the Amazon Basin in the east and the Andes Mountains in the west.

Most of the population – approximately 70% – lives in the Andes highlands between 1000-2000 meters above sea level. Colombia's river valleys, rainforest, and coastal lowlands by contrast are exceedingly hot due to the country's position on the equator. These areas are for the most part sparsely populated, with locals referring to them simply as *tierra caliente*, which literally means "hot land".

The climate is milder in the Andes Mountains, and so most of Colombia's agriculture and economic activity is centered on this region. Historically this has made Colombia more challenging to develop and govern. The Andes Mountains cut through the country in three distinct ranges, each range rising more than 5000 meters above sea level. This can make travel between Colombia's various regions exceptionally difficult. As a result, over time each region of the country developed its own economic, cultural, and political identity, and a sense of national unity has taken longer to achieve.

The Three Ranges of the Colombian Andes



Importance of new transportation infrastructure

For centuries Colombia's difficult terrain was a major hindrance to the formation of a coherent national network of trade. Construction of inter-regional highways was severely restricted, and so locals relied mostly on river boats and pack mules to move goods to market. At times they even experimented with aerial cables, the longest of which connected the city of Manizales to the Pacific coast via 45 miles of cable supported on 376 towers. By the late 20th century, perhaps the easiest way to travel throughout Colombia was by air, and so Colombia now has the 8th highest number of airports in the world (862 total).

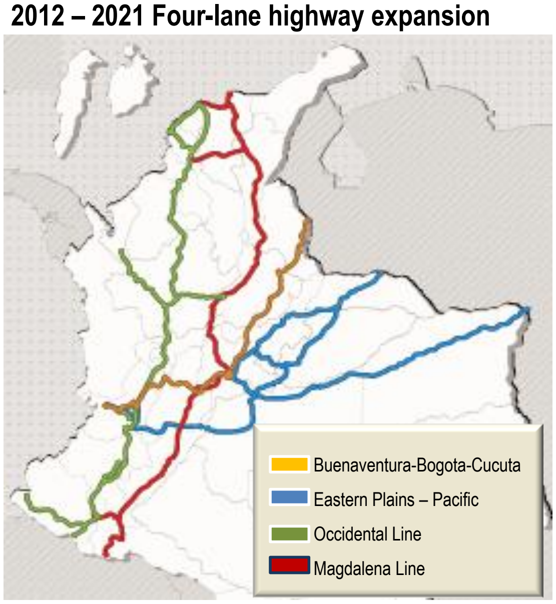
Due to this challenging geography, for most of its history Colombia has been dominated by regional economies rather than one unified national economy. Central governments in Bogotá often struggled to extend control over the various corners of the Andes. However, upcoming improvements to transportation infrastructure will help Colombia overcome many of these obstacles and likely be a key driver of economic growth over the next 10-20 years.

"Prosperity for All": National Infrastructure Plan

As part of an ongoing campaign to promote trade and economic unity, Colombia's government under the Santos Administration recently announced an aggressive new infrastructure investment plan. In 2011, Colombia spent US$3.3 billion on transportation infrastructure, or roughly 1% of GDP on a PPP basis. Through the use of Public-Private Partnerships, the government's objective is to ramp up investment to US$10 billion annually, or 3% of GDP, by 2014. As of December 2012 they are on pace to meet this target, having increased infrastructure investment to US$4.4 billion annually – a 33% increase over 2011. These funds will be used to significantly expand Colombia's highways, railroads, airports, sea ports, and maritime infrastructure.

Given Colombia's fragmented geography, the most ambitious projects involve expanding highways and railroads. Currently, most Colombian cities are connected by small, two-lane highways that snake through the mountains and make automobile travel prohibitively slow. Only 790 km of Colombia's highways are four-lanes (two lanes on each side of traffic). However, the government plans to expand four-lane highways to 5,200 km by 2021, a 6-fold increase. The railroad network will also see an additional 1,405 km of track by 2021, thereby connecting all major cities to Colombia's Atlantic and Pacific ports. Such vast improvements to civilian mobility will have transformative effects on Colombia's economy and foster a greater sense of national unity.

2012 – 2021 Four-lane highway expansion



Source: ProExport Colombia. 2012.

2012 – 2014 Port expansion

Source: ProExport Colombia. 2012.

Colombia is also planning significant improvements to its maritime infrastructure. By 2014, Colombia will spend US$1 billion to expand port capacity by 69%. This will be achieved through a combination of building new ports, expanding existing ports, and deepening access channels to accommodate larger ships. Additionally, while most of Colombia's rivers are used to transport small amounts of trade, the rivers are not commercially navigable for larger barges and ships. By 2021 the government is expected to spend US$1.7 billion to improve river navigability, thereby creating an additional 1,200 km of commercial transportation routes.

For international investors visiting Colombia, the most immediate infrastructure improvements are visible at the airports. El Dorado Airport in Bogotá is currently undergoing construction of a new terminal and control tower, both of which should be completed by 2014. This airport is already one of the largest transportation centers in South America, accounting for nearly 30% of the region's total freight. The expansion will further increase El Dorado's importance to regional trade. Improvements are expected at 23 other airports as well, and by 2014 the total number of air travelers is expected to climb to 30 million versus about 23 million in 2012. In terms of urban infrastructure, Colombia expects to spend US$3.5 billion to expand mass transit options within major cities by 2014.

POLITICAL HISTORY

Investing at the right moment in history

Since gaining independence from Spain in 1819, Colombia has endured internal or external conflict about 75% of the time, which has resulted in a society forged through great struggle and hardship. Understanding the circumstances that shaped Colombia's past will provide a better sense of what is now guiding its future – and why the future is positive.

Gran Colombia, 1819 – 1830

Source: Encyclopedia Britannica, Inc. 2012.

1810 – 1830: Cultural aversion to dictators

In 1810, the Spanish Empire was collapsing under the weight of Napoleon. Colombians were not treated kindly under Spanish rule, so on July 20 of that year Colombians declared independence. Attempts by Spain to retake the lost territory were met with fierce resistance, led by Simón Bolívar. As Spanish forces were ejected from Colombia and the surrounding area, Bolívar organized the liberated territory into a new republic known as Gran Colombia, encompassing modern day Colombia, Ecuador, Venezuela, and Panama.

This republic lasted from 1819-1828 when Bolívar, then the president, declared himself dictator. Unenthusiastic about subjecting themselves to a new monarch, the territories of Ecuador and Venezuela simply voted to secede, and by 1830 Bolívar's Gran Colombia ceased to exist. While Bolívar lamented that "America is ungovernable", his frustration stems more from Colombians' natural aversion to absolutism. Since winning independence from the Spanish crown, Colombia has strongly favored representative government, and dictatorship has never been seriously contemplated.

1831 – 1902: Cycle of conflict established

Despite their rejection of Bolívar's dictatorship, the government that emerged in Colombia after 1830 was one of a weak congress and a strong executive branch. Thus began a long back and forth struggle to reconcile competing desires for a more centralist or more federalist form of government. What typically transpired in this period was that one political party would gain power, attempt to centralize control, and the disaffected party would be left seeing violence as the only way to have a voice in the constitutional process. As a result, eight large scale civil wars were fought during this period. These conflicts tended to be regionally focused, further reflecting the challenges of forming a unified government in a country so geographically divided.

The most destructive conflict in this period was known as the War of a Thousand Days, which took place from 1899-1902. The war resulted from disagreement between the Liberal and Conservative political parties. Liberals were out of power, and had accused the Conservatives of maintaining power through fraudulent elections. The ensuing conflict claimed over 100,000 lives and devastated the entire country. Conservatives maintained power, but Colombia's weakened condition left it vulnerable to foreign intervention in 1903.

1903: Panama Canal seized by US

Panama had always considered itself disconnected from the rest of Colombia – it took 30 days for a Panamanian to travel to the capital in Bogotá. So in 1903 when the Colombian Senate rejected a US treaty to allow construction of the Panama Canal, the US did not discourage Panamanians from rebelling. US warships blocked Colombian troops from invading from either the Atlantic or the Pacific, and Panama broke away from Colombia with hardly a shot fired. It was a major national embarrassment, and a wake-up call to Colombia's political establishment.

1903 – 1948: "The New Age of Peace and Coffee"

The loss of Panama and the ease at which it slipped away was a major repudiation to Colombia's tendency for civil strife, and the whole fiasco marked a turning point as the country entered the 20th century. Government inclusion became the new norm. Conflict was replaced by a growing desire to strengthen Colombian society.

Stability was found in the form of higher coffee prices. The government began investing heavily in transportation infrastructure, and as a result by the 1920s a coffee export boom was underway. Conflict was confined to labor and land disputes, as well as a brief war with Peru over the Amazon city of Leticia.

This brief period of stability ended with the onset of the 1930s global economic depression. Like other Latin American countries of the time, Colombia turned to populist leaders to improve the plight of working class people. For Colombia, this leader was Jorge Eliécer Gaitán, whose humble lower class background resonated well with the working poor.

After a failed attempt at the presidency in 1946, Gaitán seemed poised to oust Conservative president Mariano Ospina Pérez in the 1950 election. Then on April 9, 1948, in a moment often likened to Kennedy's assassination in the US, Gaitán was murdered while campaigning in a Bogotá square. His alleged assassin was immediately killed by an angry mob, and so his motivations were never known.

1949 – 1960: La Violencia

Civil unrest was already on the rise following the Conservative victory of 1946. With Gaitán's death, riots and disorder swept the country. The ensuing period from 1946-1960 became known as *La Violencia*, or "the violence," in which an estimated 250,000 people were killed.

Amidst the turmoil, General Rojas Pinilla seized power in a military coup, establishing Colombia's first and only military dictatorship from 1953-1957. The political parties united to overthrow him and tried to restore stability. However, the success of the 1959 Cuban Revolution provided further motivation to disaffected, leftist activists. This gave rise to several militant groups such as the FARC and ELN, which remain a threat to Colombian stability to this day.

1961 – 1997: Rise of guerrillas and drug lords

The National Liberation Army, or ELN, was born out of Castro enthusiasts hoping to import the Cuban model of Communism into Colombia. The Revolutionary Armed Forces of Colombia, or FARC, formed in 1964 in response to agrarian land disputes. Yet another group, M-19, emerged in opposition to the outcome of the 1970 presidential election.

These groups committed sporadic acts of terrorism against government forces and civilians through the ensuing decades. The boldest move occurred in November 1985 when M-19 insurgents stormed the Palace of Justice in Bogotá, taking the Supreme Court hostage. Government forces, unwilling to negotiate, stormed the building. By the time the battle was over, a hundred people including eleven members of the Supreme Court had been killed.

The incident was devastating to Colombia's national morale and further emboldened militant groups. They began to actively assassinate hawkish politicians with little intervention from government forces. Kidnapping for ransom became common practice.

This lawless environment contributed to the rise of a new enemy: drug traffickers. In addition to kidnappings, militant groups found the drug trade to be particularly lucrative, and the drug cartels quickly exploited the synergy. At its peak, cocaine actually exceeded coffee as Colombia's largest export. Drug cartels became so well-financed to the point of establishing their own autonomous areas of control. As cartels battled in the streets for supremacy, Colombia became the world's murder capital.

The government launched a furious counteroffensive in 1990 after four candidates for president were assassinated, mostly on orders from drug lords. Pablo Escobar, whose Medellín cartel controlled around 80% of the global cocaine trade, was killed in 1993. By the mid-1990s, most cartels had been reduced to smaller, less-threatening *cartelitos.*

Other threats still persisted. Amidst the disorder of the 1980s, a far-right paramilitary group known as the AUC formed, this time in opposition to the leftists. By the late 1990s, the FARC and ELN were fighting the military, the AUC was fighting the FARC and ELN, and the government was fighting all three. It was hard to tell who controlled the country, and fears spread that Colombia was becoming a failed state.

1998 – 2001: "Plan Colombia"

In 1998, the fragile situation induced Colombian President Andrés Pastrana to seek help from the United States. As Clinton was leaving office, the US Congress approved an enormous US$1.35 billion aid package known as "Plan Colombia." Only Israel and Egypt were receiving more US aid at the time. This marked the beginning of Colombia's turnaround story, and laid the groundwork for a series of successes against the militant groups throughout the country.

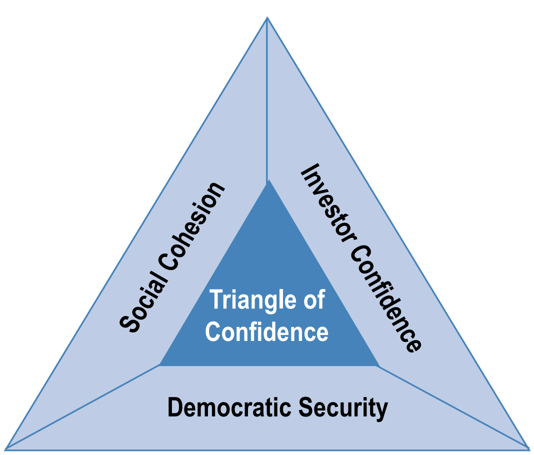
2002 – 2010: Uribe turns it around

While Pastrana gets credit for securing the aid package, it was hardline president Álvaro Uribe who finally made it bear fruit. With firm military backing from the United States, Uribe ordered a string of offensives against militant groups, and against the FARC in particular.

Uribe hoped to bring stability to Colombia through a philosophy he referred to as the "Triangle of Confidence": democratic security, investor confidence, and social cohesion. Uribe believed that improving security would also strengthen Colombia's democracy, and that investors would return to Colombia if they had full confidence in the government as a partner for business. To fully mend the country, he believed there must also be an effort to correct the social imbalances that fueled much of the civil unrest in the first place. First priority, however, would be improving Colombia's security.

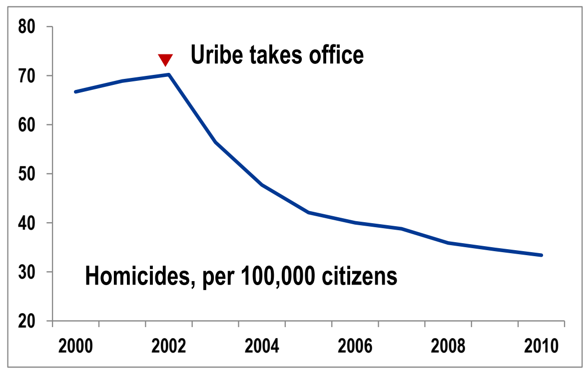
Victories were small at first, beginning with retaking Colombia's highways through use of military convoys. As the cities and highways became more secure, the militants retreated to more rural areas, mostly in the Amazon Basin.

President Uribe's "Triangle of Confidence"



The Colombian military built upon the early successes against militant groups by pursuing them into their traditional jungle safe havens. A combination of clever tactics and smart weapons technology helped the government gain the upper hand. FARC communications are now routinely intercepted, and government agents have infiltrated several of their units. By 2008, Colombia's military was conducting several operations to rescue hostages (including the famous and much-celebrated rescue of Ingrid Betancourt), as well as using precision airstrikes to eliminate the FARC leadership. By the end of Uribe's presidency, the FARC's numbers had been severely reduced - from 18,000 at its height to about 8,000 fighters in 2010. Kidnappings, once costing Colombians about US$350 million per year in ransom payments, were down by 90%, and the murder rate had fallen by half.

The Uribe Effect



Source: DANE (National Administrative Department of Statistics). 2012. The term "Uribe Effect" was originally coined by *The Economist* magazine in 2006.

2010 – Present: Peace negotiations begin

In 2010, Juan Manuel Santos succeeded Uribe as president. The same year saw many successes against the FARC, including the death of high-ranking FARC leader Mono Jojoy as well as the rescue of three hostages who had been held by the FARC for 12 years. However, with 460 government soldiers killed by FARC rebels in 2010, Colombians were reminded that the group still constituted a threat.

Following a government raid in 2011 that killed FARC leader Alfonso Cano, the militants seemed willing to enter peace talks. Santos, recognizing the government's position of strength, commenced negotiations in August 2012. Ending the conflict will likely require concessions from both sides, and full disarmament will take time. Regardless of the final terms of a deal, Santos clearly has a better chance than any of his predecessors to end the conflict and secure lasting peace.

ECONOMY AND CAPITAL MARKETS

An economy primed for growth

Despite its geographic and political divisions, Colombia's economy has been surprisingly resilient. These realities fostered an economic environment characterized by local and regional economies of scale, and over time created a culture of steady, conservative growth. Over the past 50 years, Colombia's economy has grown in real terms at an average of approximately 4% annually.

This remarkable progress is reflective not only of a country rich in resources, but also the perseverance and strength of the Colombian people. Today, the conditions for economic growth are the best in a generation. Security is improving, trust in government has been restored, and national unity is on the rise. There is a growing sense that, after 200 years of cyclical conflict and instability, Colombia has finally reached "escape velocity" and will now begin to realize its full economic potential.

Diverse set of economic drivers

The regional drivers of Colombia's economy are as diverse as the geography. The Caribbean Coast is known for tourism, logistics, and petrochemicals, and serves as Colombia's export outlet to the Atlantic Ocean. The Pacific Coast is also an important export outlet, specializing in manufacturing, agribusiness, logistics, and biotechnology. Further inland, the Central Andean region of Bogotá and Medellín is the country's manufacturing hub, while also containing some specialized agribusiness such as cut flowers. The less mountainous eastern region of Colombia, known as the Orinoquía and Amazon regions, are known mostly for agriculture, biofuels, hydrocarbons, and ecotourism.

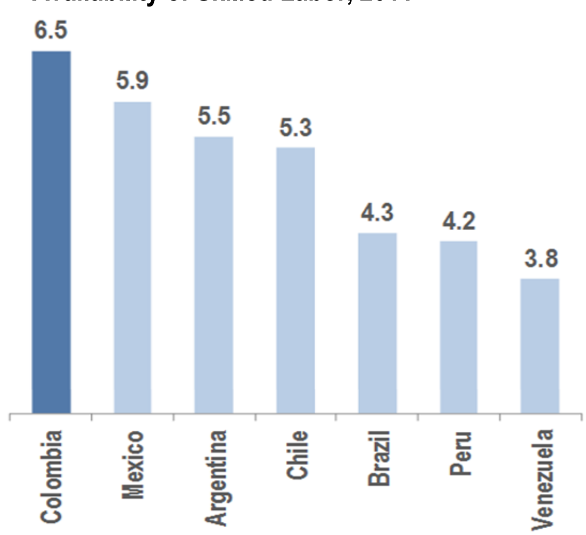
Source: ProExport Colombia, 2012.

Due to Colombia's sizeable mineral reserves, the country has greatly benefited from the recent global commodity boom, especially in its petroleum industry. The Uribe and Santos administrations have licensed large territories in Colombia's Amazon Basin to oil companies and provided them with tax breaks. They have been helped by the exodus of oil industry veterans from Venezuela, driven out by the anti-business policies of Hugo Chávez. As a result, foreign investment in Colombia's petroleum industry reached US$4.3 billion in 2011, and crude output has doubled since 2005 to a daily average of 914,000 barrels per day in 2011.

Trade has also experienced significant growth in Colombia over the past 10 years. Since 2001, exports have tripled to nearly US$57 billion in 2011, and imports have quadrupled. Colombia historically has maintained a mild current account deficit of 1%-2% of GDP, with 2011 slightly higher at 3% of GDP.

One of Colombia's greatest economic strengths is its labor force, which is considered one of the most skilled in Latin America (see below). Colombia also does an exceptional job balancing labor interests with business interests. Colombia's labor relations, flexibility, and regulations are all considered some of the best in Latin America. The credibility of management with the work force is also stronger than most of Colombia's peers, including Brazil, Chile, Mexico, and Peru. Colombia's labor force grew by 3.9% in 2011 – the 5th fastest rate of growth globally – which suggests major productivity gains ahead.

Availability of Skilled Labor, 2011



Source: IMD World Competitiveness, 2011.
Scale: 0 (low availability) – 10 (high availability)

A pro-business government

One of the three pillars of President Uribe's "Triangle of Confidence" was Investor Confidence, and that has been the guiding force for government policy towards business over the last decade. Uribe himself was known to telephone global business leaders and ask them how they could be convinced to invest in Colombia. In 2007, Uribe's administration (2002-2010) formed the Private Council for Competitiveness, an association of business leaders working to promote sound, business-friendly government regulations. Uribe's successor and current president, Juan Manuel Santos, just launched an infrastructure plan that is also expected to improve business conditions (see page 3).

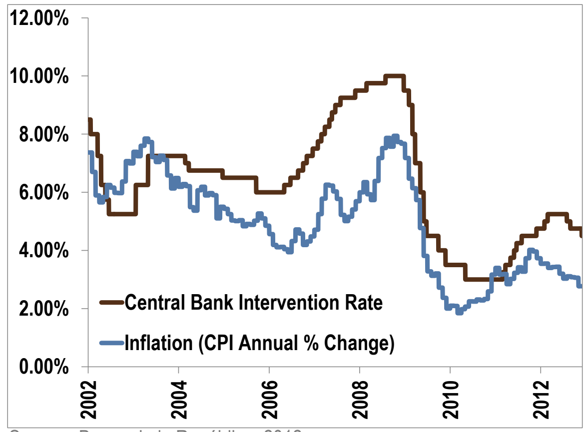
Colombia's sound fiscal policy has been favorable to business as well. The 2011 budget deficit was about 3.4% of GDP and is expected to shrink further in 2012 and 2013. As a result, all three major rating agencies recently rated Colombian sovereign debt as investment grade. The upgrade was based on several positive trends, including: 1) low debt-to-GDP compared to the developed world; and 2) historical fulfillment of obligations (Colombia has never defaulted on foreign debt).

Responsible monetary policy

The central bank of Colombia has been a reliable partner for both domestic and international investors. The bank's policy makers focus almost exclusively on inflation when setting the benchmark interest rate. They have pledged not to intervene against a strengthening Colombian Peso (currently at 1800/USD) – even if the exchange rate is hurting exports or local employment. In other words, the central bank wishes not to be a source of currency risk that might discourage foreign investment for any reason.

In addition to promoting more foreign investment in Colombia, the government's responsible monetary policy has instilled confidence in the banking sector. Armed with strong balance sheets, Colombia's banking giants have begun expanding abroad. Since 2007, the number of international branches owned by Colombian banks has increased five-fold. Much of this success stems from the financial crisis Colombia endured in the late-1990s, when interest rates soared above 40%. Following the crisis, Colombia instituted capital controls very similar to Basel III, which has resulted in healthy capital ratios.

Monetary Policy, 2002 - 2012

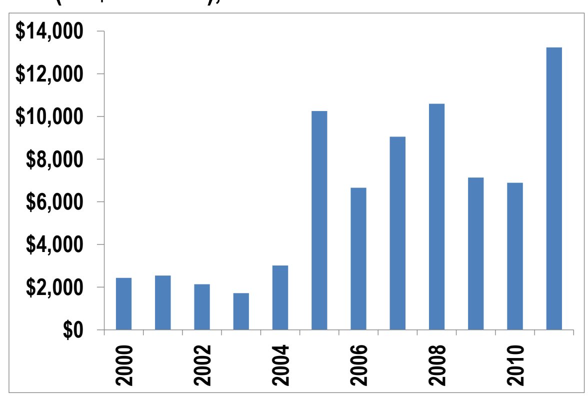


Source: Banco de la República, 2012.

Increasing foreign investment

Perhaps the most quantitative validation of government economic policy has been the increase in foreign direct investment over the last decade. Since 2002, Colombian FDI has increased by over six-fold, from US$2.1 billion in 2002 to US$13.2 billion in 2011. Some notable multinationals that are investing in Colombia today include L'Oreal, Kimberly-Clark, Unilever, DP World, Scotiabank, British American Tobacco, CFR Pharmaceuticals, and Sanofi-Aventis.

FDI (US$ millions), 2000 - 2011



Firm	Investment (US$)	Date
DP World	$150 million	Oct 2012
Scotiabank	$119 million	Aug 2012
CFR Pharmaceuticals	$194 million	Jul 2012
British Am. Tobacco	$452 million	May 2011
Unilever	$215 million	Mar 2011

Source: ProExport Colombia, 2012.

Impending benefits from free trade agreements

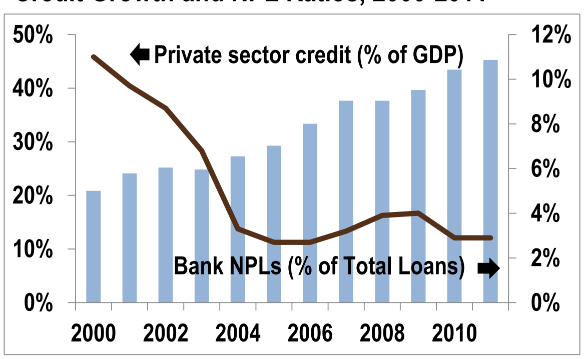
In an effort to improve Colombia's competitiveness, both the Uribe and Santos administrations have aggressively pursued free trade agreements. Most recently in Fall 2011, The US Congress ratified a new free trade agreement: the United States-Colombia Trade Promotion Agreement (CTPA).

The agreement took effect in Spring 2012, and immediately eliminates duties on 80% of US exports of consumer and industrial products to Colombia, with remaining duties to be eliminated over the next 10 years. This will provide many benefits to the Colombian economy, including increased activity in the Atlantic ports of Barranquilla and Cartagena. The US is already Colombia's leading trading partner and accounts for roughly 25% of Colombia's FDI. The CTPA will further strengthen this relationship.

Healthy capital markets

Colombia has a vibrant and developing local capital market. Banks have become more active, and domestic lending to the private sector has risen from 21% of GDP in 2000 to 45% in 2011. Banks have also managed to increase their capital ratios over the same time period, and the percentage of non-performing loans has fallen.

Credit Growth and NPL Ratios, 2000-2011



Source: The World Bank, 2012.

Colombia's public equity market has also grown over the last decade, and now exceeds US$200 billion. 2011 saw a record high nine new IPOs attracting US$7 billion. The primary exchange for public equities is the Bolsa de Valores de Colombia, or BVC. The BVC was formed in 2001 following the consolidation of the stock exchanges in Bogotá, Medellín and Occidente. Since then the total stock market capitalization as a percent of GDP has risen

US-Colombian Free Trade Zones

Source: ProExport Colombia, 2012.

from 13% to about 61% in 2011. Ecopetrol, an energy exploration firm, is by far the largest company in Colombia and accounts for 45% of the BVC's market cap. In 2010, BVC merged with the Peruvian and Chilean stock exchanges to form the Mercado Integrado Latinoamericano, or MILA, which has led to greater liquidity and sources of funding.

The most widely adopted benchmark for Colombian equities specifically is the IGBC index, consisting of 37 of the BVC's most liquid names such as Ecopetrol, BanColombia, and Grupo Inversiones. However, like the rest of the Colombian equity market, the IGBC is not very diversified. Nearly 50% of the index is weighted to Oil & Gas, with Financial Services being the second highest with 32%. The ten largest companies represent approximately 80% of market cap, which is much higher than other comparable Latin American indices.

For these reasons, private investments tend to offer better diversification for international investors looking to gain exposure to Colombia's broad growth and emerging middle class. The industry is still in its early stages. Colombia's first private equity regulations went into effect six years ago, which created a local fund structure. In 2011 the government granted permission for local pension funds to invest as much as 10% of their AUM in private equity. As of September 2012, there were 23 active Colombia-based private equity funds investing an aggregate US$2.2 billion.

REAL ESTATE MARKET

Opportunity in an emerging asset class

The attractive fundamentals shaping the macro economy in Colombia should also create significant opportunities in local real estate. As more multinational companies establish operations in Colombia, demand for office space will increase. This provides an opportunity for developers, as most of Colombia's current supply of office space does not conform to international standards. Bogotá has a particularly large shortage of office space. At 1.7 million square meters of GLA, the city has one of the lowest office penetration rates of any major Latin American city.

Colombians' purchasing power has increased by over 60% in the past decade, with the increased consumption creating a need for more shopping centers. Shopping center penetration in Bogotá, relative to population, is 30% less than peer cities such as Santiago, Mexico City, or Sao Paolo. Vacancy in existing shopping centers is nearly zero, suggesting a strong need for additional supply. However, the retail sector has high barriers to entry, especially for larger scale shopping malls, and few developers possess the capital or expertise to complete new projects.

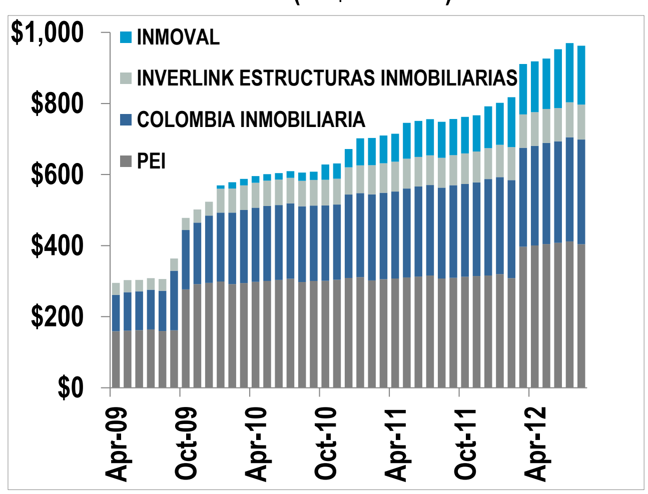
The growing purchasing power of the middle class has also led to changing tastes in housing. Colombia has a housing deficit of about 2 million units. With affordability on the rise, more Colombians will have the means to access better quality housing. Mortgage penetration is also very low at about 2.8% of GDP, and growth in consumer lending should also provide demand support. For developers, housing construction in Colombia has a unique element of downside protection, as construction is only allowed to begin after reaching a specified pre-sales target of 50-70%. The pre-sales also result in a shorter investment cycle, which allows for capital to be recycled much faster.

Increased trade and improved security should lead to more tourism and business travel, fueling demand in the hospitality sector. Since Uribe instituted business and security reforms in 2002, annual foreign visits to Colombia have increased by 140%. As a result, several multinational hotel chains such as Starwood, Marriott, Hyatt, and Four Seasons have been expanding throughout Colombia's major cities.

Colombia's logistics and industrial sectors will benefit from new infrastructure investments such as the expansion of ports and airports, as well as the increased economic activity provided by the US-Colombian Free Trade Agreement. Bogotá's El Dorado airport, for example, accounts for nearly 30% of total freight in South America and is undergoing expansion. Logistics facilities near the airport currently have no vacancy and command some of the highest rents in the country.

As a result of these positive fundamentals, Colombian real estate is now emerging as an institutionally suitable asset class. As part of the 2011 pension reforms, the government now allows local pensions to invest up to 5% of their assets in real estate. A handful of real estate funds, backed mostly by pension fund money, have started building portfolios throughout the country, with total AUM now approaching $1 billion. As of August 2012, Terranum Investment's Patrimonio Estrategias Inmobiliarias, or PEI, was the largest real estate fund in the market. The fund is structured similarly to an American REIT, and manages US$404 million invested across 21 properties.

Real Estate Fund AUM (US$ millions)



Source: Superintendencia Financiera de Colombia, Economist Intelligence Unit, 2012.

Growing need for new development

Due to an impending transition in the structure of Colombia's real estate market, one of the best investment opportunities over the coming decades will likely be in new development. During Colombia's 1999 financial crisis when interest rates exceeded 40%, developers coped by financing new projects with pre-sales. As this practice became more commonplace, government regulations were enacted mandating that pre-sale proceeds must be deposited in a third party managed trust. The trust would only release these proceeds after reaching a "point of equilibrium" in sales, generally ranging from 50%-70% of total units.

As a result, the vast majority of modern developments in Colombia have typically been strata-title "develop-for-sale". Even traditional lease assets such as shopping centers have been pre-sold on a store-by-store basis, with only 4% of national shopping center GLA controlled through centralized ownership.

A shift is now underway, with a renewed appetite for "develop-to-lease" strategies particularly in the retail, office, and industrial sectors. Pension funds are driving the trend somewhat as they seek stabilized, yield-producing assets. However, available supply is limited, and several newly formed investment funds and REITs have been scouring the market in search of these core assets. Developers are taking note and changing their business models to accommodate the demand.

Colombia's supply / demand characteristics also support the case for new development as a profitable strategy. Bogotá, for instance, despite being one of the largest cities in Latin America, has a severe shortage of Class A office space, and most of the existing supply is strata-title. Shopping center penetration is also low relative to peer countries, and occupancy of existing retail developments remains high.

Improvements in capital markets have finally made develop-to-lease commercially viable, but the equity required is much larger due to the absence of pre-sales. As a result, there is a growing opportunity for foreign capital to fill the void.

In Closing

Colombia is a nation in transition. For hundreds of years, its broken geography has prohibited it from achieving political stability and realizing its full economic potential. This is finally changing. New infrastructure is pulling the country together into a single political and economic community. Improved security and pro-business policies are bringing back foreign investment. An emerging middle class is fueling consumption and improving standards of living throughout the country. Colombia still has many problems that will require work in the years ahead, but the trend is clear: Colombia is heading in the right direction.

Investors have several available options to capitalize on Colombia's emergence, and real estate development is among the most attractive. The real estate market is in the early stages of becoming more institutionalized. Increased demand for top quality assets, both from strategic and financial investors, will support this trend in the years ahead. Colombia's real estate market presents a unique window of opportunity, and investors entering today should be handsomely rewarded.

REFERENCES

Arias, Andres F. "The Colombian Banking Crisis: Macroeconomic Consequences and What to Expect." August 2000. Web. 2 December 2012 < http://quimbaya.banrep.gov.co/docum/ftp/borra157.pdf>.

Bolsa de Valores de Colombia. Market Capitalization. 8 December 2012. Web. 8 December 2012 <http://en.bvc.com.co/pps/tibco/portalbvc>.

Central Intelligence Agency. *The World Factbook: Colombia*. 4 December 2012. Web. 6 December 2012 <https://www.cia.gov/library/publications/the-world-factbook/geos/co.html>.

"Colombia's oil industry: Gusher and guns." *The Economist.* 17 March 2012. Web. 15 November 2012. <http://www.economist.com/node/21550304>.

IMD. *World Competitiveness Yearbook 2011.* 2011. Web. 2 December 2012. <http://www.imd.org/research/publications/wcy/index.cfm>.

LaRosa, Michael J. and German R. Mejia. *Colombia: A Concise Contemporary History*. United Kingdom: Rowman & Littlefield Publishers, Inc; 2012. Print.

Latin American Private Equity & Venture Capital Association. "Executive Briefing: PE Players Take the Field in Colombia." *Latin American Private Equity & Venture Capital Association.* 29 November 2012. Web. 6 December 2012 <http://lavca.org/2012/11/29/executive-briefing-pe-players-take-the-field-in-colombia/>.

United Nations, Department of Economic and Social Affairs, Population Division. *World Population Prospects: The 2010 Revision, CD-ROM Edition.* April 2011. Web. 2 December 2012. < http://esa.un.org/wpp/Excel-Data/population.htm>.

United Nations, Office on Drugs and Crime. 2011 Global Study on Homicide. 2011. Web. 7 July 2012 < http://www.unodc.org/unodc/en/data-and-analysis/statistics/crime/global-study-on-homicide-2011.html>.

Vélez, Álvaro Uribe. *No Lost Causes.* New York, NY: Penguin Group (USA) Inc.; 2012. Print.

The World Bank. *World dataBank.* 31 October 2012. Web. 8 December 2012 <http://data.worldbank.org/>.

The World Bank: Doing Business. "Colombia: sustaining reforms over time." 2011. Web. 2 December 2012 <http://www.doingbusiness.org/~/media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB13-Chapters/DB13-CS-Colombia.pdf>.

RECOMMENDED READING

Colombia: A Concise Contemporary History by Michael J. LaRosa and German R. Mejia

No Lost Causes by Álvaro Uribe Vélez

Park Madison Partners is a boutique New York-based real estate capital raising and advisory firm focused on the global real estate private equity and alternative investments industry. Since its formation in 2006, Park Madison has participated in the placement of over $4 billion in real estate equity capital.

For more information, please visit www.parkmadisonpartners.com.

Disclaimer

200 Harbor Rd, Port Washington, NY 11050 • 1120 Avenue of the Americas, Suite 1808, New York, NY 10036
Main 212.626.6526 Fax 212.626.6527 • www.parkmadisonpartners.com • Member FINRA